1999 Country Reports on Economic Policy and Trade Practices
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REPUBLIC OF KOREA

Key Economic Indicators

(Millions of U.S. Dollars unless otherwise indicated)

	1997	1998	1999 1/
Income, Production and Employment:			
GDP (nominal/factor cost)	476,600	321,300	408,800
Real GDP Growth (pct) 2/	5.0	-5.8	7.0
GDP by Sector:			
Agriculture/Fisheries	25,505	15,768	18,750
Manufacturing	137,702	98,521	138,300
Electricity/Gas/Water	10,098	7,519	9,380
Construction	55,510	32,560	35,800
Financial Services	91,146	62,886	81,500
Government/Health/Education	36,436	25,864	22,000
Other	120,203	78,182	103,070
Government Expenditure (pct/GDP)	22.1	23.4	22.5
Per Capita GDP (US$)	10,307	6,823	8,735
Labor Force (000s)	21,500	21,800	22,000
Unemployment Rate (pct)	2.5	7.4	4.5
Money and Prices (annual percentage rate):			
Money Supply (M2)	19.2	24.0	25.0
Corporate Bonds 3/	13.4	15.1	8.5
Personal Savings Rate	22.8	25.1	25.5
Retail Inflation	4.5	7.5	2.0
Wholesale Inflation	3.9	12.2	1.0
Consumer Price Index (1995 base)	109.6	117.8	120.2
Average Exchange Rate (Won/US$)	951.1	1,399	1,200
Balance of Payments and Trade:			
Total Exports FOB 4/	136,164	132,313	137,000
Exports to U.S. 4/	21,625	22,805	24,000
Total Imports CIF 4/	-144,616	-93,282	-115,000
Imports from U.S. 4/	-30,122	-20,403	-25,000
External Debt 5/	159,200	148,700	138,000

Debt Service Payments	-18,000	-29,800	-24,000
Gold and FOREX Reserves	20,406	52,041	65,000

1/ 1999 figures are estimates based on available monthly data as of October.
2/ Growth based on won, the local currency.
3/ Figures are average annual interest rates.
4/ Merchandise trade, measured on customs clearance basis; Korean government data.-
5/ Gross debt; includes non-guaranteed private debt.

1. General Policy Framework

South Korea demonstrated its resilience and its capacity for change by bouncing back strongly in 1999 from the 1997-98 economic crisis, the worst in the country's history. After experiencing a 5.8 percent contraction in 1998, 7 to 8 percent GDP growth is forecast in 1999. Per capita GNP in dollar terms will be $8,735 in 1999, up from 1998's $6,823 but still lower than $10,307 in 1997.

The crisis called into question the viability of a growth model that relied heavily on a protected domestic market and the deep involvement of the government in determining the allocation of capital. The crisis also set the scene for the presidential election victory in December 1997 of opposition figure and economic reform advocate Kim Dae Jung.

By mid-1998, largely due to the $58 billion IMF program that Korea entered into in December 1997 and President Kim's commitment to vigorous financial and corporate sector reform, stability was restored to the Korean economy. However, problems remain with respect to implementation of reform and restructuring measures in these two sectors. Although the Korean government has made progress in inducing the conglomerates ("chaebols") to reduce their unsustainable debt/equity ratios, to improve corporate governance and enhance transparency, and to restructure their operations, the chaebol have only partially implemented Republic of Korea (ROK) government-mandated changes in these areas. In general, Korean business preference for market share instead of profitability and an unrealistically low Korean bankruptcy rate encouraged over-capacity and corporate inefficiency, but discouraged investment in small-to-medium enterprises (SME's). The SME sector remains underdeveloped in Korea.

In 1999 the chronic de facto bankruptcy of Daewoo, the second-largest Korean conglomerate, and continued weakness in the financial sector, especially the over-leveraged investment trust companies (ITC's), showed the weakness of the past patterns of misallocation of investment resources, excessive debt, and lack of effective oversight. The Daewoo crisis became front-page news around the world in July 1999, as that massive firm with far-flung global interests and investments came near default on more than $50 billion in debt. That month, creditors rolled over 12 trillion won in debt that was coming due over the following 10 days. Meanwhile, the $200-billion-plus ITC industry faced a loss of investor confidence due to its exposure to Daewoo and the lack of adequate prudential supervision. The Korean government's handling of the twin Daewoo and ITC crises will be a litmus test of its resolve to see through meaningful and sustainable corporate reform and restructuring, as well as the key to reducing systemic risk in the economy.

Korea produces and exports advanced electronic components, automobiles, steel, and a wide variety of mid-level, medium-quality consumer electronics and other goods. As labor activism in the 1980's drove up wages faster than productivity growth, Korea lost its low-wage labor advantage to China and Southeast Asian countries. At the same time, Korea faced tough competition from Japan in cutting-edge, high-tech products.

Aided by recovery in other Asian markets and a strong current account surplus, Korea’s usable foreign currency reserves in 1999 grew to over $60 billion, while the Korean won stabilized at about 1,200/dollar as of November 1999. (The won stood at 900/dollar in 1996 but by late 1997 had dropped as low as 1,960/dollar). Korea became a member of the OECD in December 1996. Inflation dropped to about two percent in 1999.

Facility investment is expected to grow 34 percent in 1999, after suffering a 38 percent fall in 1998. In 1999, the unemployment rate is expected to drop to around 4.5 percent with less than one million unemployed people, a fall from seven percent in 1998 when there were over 1.4 million jobless. Real income grew eight percent during the first seven months of 1999 after a nine percent fall in 1998. Private consumption grew 8.2 percent in 1999. (Expenditures on domestic consumption accounted for 62 percent of total GDP.)

The United States is Korea’s leading trade partner in 1999, taking 20 percent of Korea’s exports and providing 21.7 percent of Korea’s imports for the first nine months of 1999. Korea is the eighth largest overall trade partner of the United States (the sixth biggest market for U.S. exports and the eighth biggest for U.S. imports) up from ninth in 1998. U.S. Commerce Department statistics show that, through September 1999, U.S. exports to Korea increased 52.2 percent to $16.9 billion, and U.S. imports from Korea rose 25.8 percent to $22.2 billion. In 1998 U.S. exports to Korea fell 34 percent while U.S. imports from Korea rose 3.4 percent.

The public sector’s role in the economy is relatively small, with taxes and expenditures amounting to 24 percent of GDP in 1999. The government plans to increase nominal budget spending five percent in 2000 (the lowest budget growth since 1992) for economic stimulus, to improve and expand transportation infrastructure, and to improve the social safety net for the unemployed. The 2000 fiscal deficit is expected to be about 3.5 percent of GDP, somewhat less than four percent in 1999. About 12 percent of 2000 spending will be financed by government bond sales. In 1998 the government increased the money supply about 20 percent to fight potential deflation due to the recession and falling asset values. In consultation with the IMF, the government allowed the overnight call rate, which is the main policy interest rate of the Bank of Korea, to fall from a peak of 35 percent in December 1997 to single digits in 1999. In September 1999, however, corporate bond rates rose sharply above 10 percent when Daewoo’s financial default destabilized the bond market and investors rushed to withdraw money from financially weak investment trust companies. However, the ROK reversed the rise in long-term rates in October with its bond market stabilization fund. The primary monetary target of the Bank of Korea is M3, which, in accordance with Korea's IMF program, is expected to increase by about 11 percent in 1999.

2. Exchange Rate Policy

Since the introduction of the IMF program in December 1997, foreign exchange and capital controls have been relaxed or abolished. In conjunction with IMF program requirements that the exchange rate be allowed to float (with intervention limited to smoothing operations only.) In December 1997 the exchange rate peg was widened from +/- 2.25 percent to +/- 10 percent, and then abandoned completely.

3. Structural Policies

The Korean economic model has been notable for the high degree of concentration of capital and industrial output in a small number of conglomerates known as "chaebol." While this model produced a long record of high economic growth, the 1997 financial crisis exposed its weaknesses, which include excessively risky debt levels, industrial over-capacity, and economically unsustainable investment. President Kim Dae Jung has pushed for major economic reform and restructuring to overcome these shortcomings. The government passed laws requiring greater corporate transparency, strengthened prudential requirements for banks and other financial institutions, fostered the development of small and medium-sized industries, and encouraged increased foreign investment in Korea. The chaebol have also been pressed to restructure and rationalize their operations, including by reducing their debt/equity levels to 200 percent and through somewhat controversial "big deals" (i.e. asset/affiliate swaps.) The effective and radical restructuring of Korea's second-largest chaebol Daewoo should help accelerate the pace of corporate reform. These reforms are moving Korea's economy towards a more market-based system, but some important changes, especially in the financial and corporate sectors, will take time.

4. Debt Management Policies

Korea's total foreign debt (largely private sector) totaled $144 billion at the end of July 1999, declining from $158 billion at the end of 1997. Through repayment and rescheduling, Korea's short-term debt as a percentage of total debt has been reduced from 64 percent at the end of 1998 to only 24 percent at the end of July 1999. In addition, the ROK developed an external debt reporting system to enhance debt management and monitoring. Through September 1999, Korea registered a current account surplus of $19.2 billion, substantially smaller than the $32 billion surplus recorded during the comparable period a year before. The estimated surplus for 1999 is $20 billion, compared to about $40 billion in 1998.

5. Significant Barriers to U.S. Exports

During the last decade Korea has gradually liberalized its markets for both goods and services and improved its investment climate for U.S. and other foreign firms. Through bilateral and multilateral efforts, many protective tariffs were lowered or phased out. Non-transparent policies and regulations, which directly or indirectly inhibited market access for imports, have been revised and reduced. The ROK has distanced itself from explicit policies that encouraged anti-import sentiment among Korean consumers, and is slowly addressing residual anti-import biases among both Korean consumers and bureaucrats. Rather than tolerating some foreign investment as necessary, the ROK has introduced a new foreign investment regime and is actively working to attract foreign investment. Korea and the United States initiated negotiations in June 1998 to conclude a bilateral investment treaty. Total commitments of foreign direct investment in 1999 is expected to exceed $15 billion, more than double the level in 1997. Nevertheless, these improvements have not benefited all exporters to Korea and barriers to exports from the United States and other countries continue to plague key sectors, especially agriculture, pharmaceuticals and automobiles.

In general, Korea's tariffs are modest; Korea's average tariff rate is 7.9 percent. However, Korea still maintains a system of high tariffs (30 to 100 percent), quotas and tariff rate quotas (TRQ), mostly for sensitive agricultural and fishery products of interest to U.S. suppliers, which effectively restrict imports. In addition, Korea's administration of quotas/TRQs for some products, such as rice and oranges, limits legitimate market access. Korea also uses adjustment tariffs to respond to import surges; however, the number of these tariffs is slowly being reduced. The majority of the remaining 29 adjustment tariffs apply to agricultural products. The government eliminated its import diversification program, which barred certain imports from Japan, in June 1999, and has committed to phase out its eight GATT balance of payments restrictions by year-end 2000.

Nontariff barriers, which often result from non-transparent regulatory practices, continue to inhibit imports to Korea across a range of sectors. A lack of regulatory transparency and consistency can affect licensing, inspections, type approval, marking/labeling requirements and other standards. To add transparency and due process to its regulatory system, Korea enacted the Administrative Procedures Act in 1996, but public notice of new regulations, as well as comment and transition periods are not always adequate. The regulatory system has not offered adequate recourse to those adversely affected by creation of new regulations. Since President Kim initiated a comprehensive regulatory review in 1998, more than 5,000 regulations/guidelines have been eliminated or targeted for elimination; review of the more than 6,000 remaining regulations is ongoing.

Products regulated for health and safety reasons (such as pharmaceuticals, medical devices, and cosmetics) typically require additional testing or certification from the relevant ministries before they can be sold in Korea, resulting in considerable delays and increasing costs. The foreign pharmaceutical industry faces discriminatory barriers associated with clinical registration and reimbursement pricing issues, although a new reimbursement pricing system is expected to be implemented in late 1999. Registration requirements for such products as chemicals, processed food, medical devices and cosmetics hamper entry into the market as well. Korea has initiated efforts to streamline its complex and burdensome import clearance procedures, targeting some 54 laws for revision. It has committed to bring its Food Code, Food Additive Code and labeling requirements into conformity with international standards. Import clearance, however, still takes longer than in other Asian countries.

Despite potential conflict of interest problems, the government has delegated authority to some Korean trade associations to carry out functions normally administered by the government. Such delegation of responsibility may include processing import approval documentation prior to customs clearance (allowing local trade associations to obtain business confidential information on incoming shipments), advertisement pre-approvals (providing early warning on the introduction of new products and on competitors' marketing efforts), and a decision-making seat on various committees (usually not available to foreign firms). The Korea Fair Trade Commission increased its efforts in 1999 to reduce the quasi-legal, trade restrictive powers of a number of associations.

The United States and Korea signed a Memorandum of Understanding (MOU) in October 1998, in which Korea agreed to take measures to further open its automobile market and improve market access for U.S. automobiles. Per the MOU, Korea has lowered some taxes which had a discriminatory impact on imported cars, bound its auto tariffs at 8 percent, improved consumer financing of autos by expanding the auto mortgage system and shortening the repossession process, and streamlined standards and certification. The ROK has also taken steps to reduce anti-import attitudes, which have an especially strong impact on foreign automobiles, including by agreeing to co-sponsor an "Import Motor Show" in May 2000. Despite these efforts, imports of U.S. and other foreign cars will barely exceed 2000 units in 1999.

The government requires theaters to show local movies for a minimum of 146 days each year, with some flexibility so that this total can be reduced to 106 days. U.S. industry states that these constraints on foreign movies and programs are more restrictive than in most other countries. The Korean government, however, considers this a cultural rather than a trade issue.

Korea acceded to the WTO Government Procurement Agreement (GPA) on January 1, 1997 and is co-sponsoring the Transparency in Government Procurement initiative in the WTO. U.S. firms, however, continue to raise some concerns about Korean procurement practices, including discrimination against U.S. firms participating in procurements for Korea's new international airport conducted by the Korea Airport Construction Authority. The U.S. government is currently pursuing WTO dispute settlement resolution on this issue with Korea.

Korea will expand its Uruguay Round minimum import quota for beef to 225,000 metric tons by the year 2000 and expand the proportion of the quota imported through the "simultaneous buy/sell system." Korea has committed to remove all remaining nontariff barriers to beef imports, including state trading, by January 2001. However, due to a sharp drop in consumption, Korea has been unable to meet its WTO minimum import commitment in recent years. In February 1999, the United States initiated WTO dispute settlement consultations with Korea to eliminate import barriers and distribution restrictions on foreign beef.

In response to the 1997 financial crisis, the government has implemented broad-based reforms of its financial system. These reforms include substantial liberalization of capital markets, including the abolition of restrictions on foreign ownership of domestic shares and bonds, and restrictions on the use of deferred payments to finance imports. Foreign banks can now establish subsidiaries in Korea and foreign financial firms can participate in mergers and acquisitions of domestic Korean financial institutions. Korea, however, requires foreign branches to be separately capitalized, and other regulations such as prudential lending limits are based on local branch capital as opposed to its total capital, while a domestic bank's capital base is assessed as the entire bank's capital. Foreign banks are also disadvantaged in access to local currency funding. The government has also loosened controls over access to currency, such as swap lines used by banks as a source of local currency, but the government retains controls and has not committed to maintaining these new lines once the crisis is over. The new Foreign Exchange Transaction Law that was implemented in April 1999 significantly liberalized formerly heavily regulated capital transactions.

Korea' new Foreign Investment Promotion Act, which became effective in 1998, streamlined foreign investment application procedures and eased barriers to foreign direct investment across a range of sectors. Korea now has a much more favorable investment climate for foreign firms, and in the longer run this should foster broader market access and more imports. Investment restrictions now remain on only 21 industrial sectors, of which seven are entirely closed. Mergers, including hostile mergers, are allowed, and most restrictions on foreign ownership of local shares have been lifted. Foreigners are now allowed to purchase real estate and property. Tax incentives, especially for the high technology sector, have been increased. Restrictions on access to offshore funding (including offshore borrowing, intra-company transfers and inter-company loans), however, continue to be burdensome. Foreign equity participation limits, licensing requirements and other regulatory restrictions can limit foreign direct investment in sectors nominally open to foreigners. Foreign firms also face additional investment restrictions in many professional services sectors.

6. Export Subsidies Policies

In the past, Korea aggressively promoted exports through a variety of policy tools, including export subsidies, directed credit and targeted industrial policy. However, in the WTO, Korea has committed to phasing out those programs not permitted under the WTO Agreement on Subsidies and Countervailing Measures. Under the IMF stabilization package, Korea eliminated four WTO prohibited subsidies. The real benefit of the few remaining subsidized lines of export credit is insignificant in a macroeconomic sense. The relative size of direct grants is small and declining with regard to both the government budget and growing private investment. The use of tax exemptions, the main vehicle for export promotion, appears to be declining as well. The government does expend large amounts of money in research and development in key industrial sectors targeted for development, such as telecommunications.

7. Protection of U.S. Intellectual Property

Korea is a participant in the WTO's Agreement on Trade Related Aspects of Intellectual Property (TRIPs). It is also a signatory to the World Intellectual Property Organization

(WIPO), the Universal Copyright Convention, the Budapest Treaty on the International Recognition of the Deposit of Microorganisms, the Geneva Phonograms Convention, the Paris Convention for the Protection of Industrial Property, and the Patent Cooperation Treaty. Korea joined the Berne Convention in August 1996.

Korean laws protecting IPR are generally adequate in legal terms, but problems remain with respect to enforcement. Korea's Special 301 status was downgraded from "Priority Watch List" to "Watch List" in April 1997. Korea maintained its "Watch List" status in the U.S. government's 1999 review. Areas of continuing IPR concern include: counterfeit consumer products, software piracy, and pharmaceutical patent protection enforcement.

Korean patent law is fairly comprehensive, offering protection to most products and technologies. A new patent court came into effect March 1, 1998. However, approved patents of foreign patent holders are still vulnerable to infringement. Korean law provides for compulsory licensing of patents when the invention is deemed necessary for the national defense, for the public interest, or for the protection of a dependent patent.

The government's protection of trademarks has improved since 1991. A revised Trademark Law became effective March 1, 1998. The Design Act was also revised on March 1, 1998, enhancing protection of industrial designs. The granting of a trademark under Korean law is based on a "first-to-file" basis. While preemptive and predatory filings are on the decline, "sleeper" preemptive registrations still surface on occasion. A new provision now allows the Korean Industrial Property Office (KIPO) to reject suspected predatory applications based on a "bad faith" clause. There has been less success in stemming the export of Korean counterfeit products globally.

Korea's Copyright Law protects author's rights, but local prosecutors take no action unless the copyright holder files a formal complaint. In 1999, Korea amended its Computer Program Protection Act and is preparing revised copyright legislation so as to better meet its TRIPs obligations, especially with respect to copyright and trademark protection for transactions conducted on the internet. Korea, however, is not in full compliance with provisions of the TRIPs Agreement which stipulate that preexisting works and sound recordings must enjoy a full term of protection (i.e., life of the author plus 50 years for works; 50 years for sound recordings). Korea now only provides protection back to 1957. The Korean government in 1999 has devoted increased resources and staff to IPR enforcement activities and President Kim himself has directed cabinet agencies to step-up government efforts to protect intellectual property. However, IPR violations, especially of computer software, including in the government sector remain a problem.

8. Worker Rights

a. The Right of Association: With the exception of public sector employees and teachers, Korean workers enjoy the right of free association. White-collar workers in the government sector cannot join unions, but blue-collar employees in the postal service, railways, and telecommunications sectors, and the national medical center have formed labor organizations. Starting this year, government employees were allowed to form workplace consultative councils. In July, legislation went into effect allowing teachers to form unions. Unions may be formed with as few as two members and without a vote of the full prospective membership.

Until recently the Trade Union Law specified that only one union was permitted at a workplace, but labor law changes in 1997 authorize the formation of competing labor organizations beginning in the year 2002. Workers in government agencies and defense industries do not have the right to strike. Unions in enterprises determined to be of "essential public interest," including utilities, public health, and telecommunications, may be ordered to submit to government-ordered arbitration in lieu of striking. In fact, work stoppages occur even in these sensitive sectors. The Labor Dispute Adjustment Act requires unions to notify the Labor Ministry of their intention to strike, and normally mandates a 10-day "cooling-off period" before a work stoppage may legally begin.

b. The Right to Organize and Bargain Collectively: The Korean constitution and the Trade Union Law provide for the right of workers to bargain collectively and undertake collective action, but does not grant government employees, school teachers or workers in defense industries the right to strike. Collective bargaining is practiced extensively in virtually all sectors of the Korean economy. The central and local labor commissions form a semi-autonomous agency that adjudicates disputes in accordance with the Labor Dispute Adjustment Law. This law empowers workers to file complaints of unfair labor practices against employers who interfere with union organizing or practice discrimination against unionists. In 1998 the government established the Tripartite Commission, with representatives from labor, management, and the government to deal with labor issues related to the economic downturn. The work of the Commission both made it legal for companies to lay off workers due to economic hardship and authorized temporary manpower agencies. Labor-management antagonism, however, remains an issue, and some major employers remain strongly antiunion.

c. Prohibition of Forced or Compulsory Labor: The constitution provides that no person shall be punished, placed under preventive restrictions, or subjected to involuntary labor, except as provided by law and through lawful procedures. Forced or compulsory labor is not condoned by the government and rarely occurs.

d. Minimum Age for Employment of Children: The government prohibits forced and bonded child labor and enforces this prohibition effectively. The Labor Standards Law prohibits the employment of persons under the age of 15 without a special employment certificate from the Labor Ministry. Because education is compulsory through middle school (about age 14), few special employment certificates are issued for full-time employment. Some children are allowed to do part-time jobs such as selling newspapers. In order to obtain employment, children under 18 must have written approval from their parents or guardians. Employers may require minors to work only a limited number of overtime hours and are prohibited from employing them at night without special permission from the Labor Ministry.

e. Acceptable Conditions of Work: The government implemented a minimum wage in 1988 that is adjusted annually. The minimum wage in 1998 was set at $1.28/hour (won 1,525/hour). Companies with fewer than 10 employees are exempt from this law. The maximum regular workweek is 44 hours, with provision for overtime to be compensated at a higher wage, but such rules are sometimes ignored, especially by small-companies. The law also provides for a maximum 56-hour workweek and a 24-hour rest period each week. Labor laws were revised in 1997 to establish a flexible hours system that allows employers to ask laborers to work up to 48 hours during certain weeks without paying overtime so long as average weekly hours do not exceed 44. The government's health and safety standards are not always effectively enforced, but the accident rate continues to decline. The number of work-related deaths remains high by international standards.

f. Rights in Sectors with U.S. Investment: U.S. investment in Korea is concentrated in petroleum, chemicals and related products, transportation equipment, processed food, manufacturing and services. Workers in these industrial sectors enjoy the same legal rights of association and collective bargaining as workers in other industries.

Extent of U.S. Investment in Selected Industries -- U.S. Direct Investment Position Abroad on an Historical Cost Basis **--** 1998

(Millions of U.S. Dollars)

Category		Amount
Petroleum		(1)
Total Manufacturing		2,940
Food & Kindred Products	380	
Chemicals & Allied Products	530	
Primary & Fabricated Metals	22	
Industrial Machinery and Equipment	288	
Electric & Electronic Equipment	558	
Transportation Equipment	128	
Other Manufacturing	1,034	
Wholesale Trade		(1)
Banking		2,251
Finance/Insurance/Real Estate		38
Services		446
Other Industries		-38
TOTAL ALL INDUSTRIES		7,365

(1) Suppressed to avoid disclosing data of individual companies.

Source: U.S. Department of Commerce, Bureau of Economic Analysis.